Jardine Lloyd Thompson Sdn Bhd v Berjaya Sompo Insurance Bhd

COURT OF APPEAL (PUTRAJAYA) — CIVIL APPEAL NO W-02(NCC)(W)-2036–09 OF 2013
ZAHARAH IBRAHIM, ANANTHAM KASINATHER AND VARGHESE GEORGE JJCA
25 MARCH 2014

Insurance — Construction of policy — Exemption clause — Insurance policy provided for insurer to indemnify insured against claims by clients for loss arising from fraudulent conduct of insured's employees — Claims for loss of money and five other specified items not covered by indemnity — Insurer refused to indemnify when insured to make good loss suffered by client arising from its employee's fraud — Whether High Court wrong to hold insurer right on ground insured's claim was claim for 'loss of moneys' — Whether High Court's interpretation denied insured of very peril it had insured against

The appellant ('JLT') was an insurance broker which had purchased a professional indemnity insurance policy from the respondent to be indemnified if claims were brought against JLT by its clients. An employee of JLT ('Razak') fraudulently caused JLT's client, a bank, to overpay on insurance premiums which went into third-party accounts to which Razak had access. On discovering the fraud, the bank demanded and recovered from JLT the excess premiums it had paid. JLT sought indemnity from the respondent on the bank's claim but the respondent repudiated liability leading to the instant action. The determination of the dispute between the parties under O 14A of the Rules of Court 2012 turned on the construction of the professional indemnity policy. Clause 1(b) of the policy provided that JLT would not be indemnified if the claims made against it were, inter alia, brought about or contributed to by JLT's 'dishonest, fraudulent, criminal, malicious or deliberate act, error or omission'. The clause also provided that there would be no indemnity for claims made for 'loss of money' and other specified items which were in JLT's care or custody. JLT purchased an optional extension clause which provided that cl 1(b) would not apply where the claims made against JLT arose out of or were contributed to 'by the dishonest, fraudulent, malicious or deliberate conduct' of its employees. The optional extension clause, however, did not cover claims 'arising out of or in connection with loss of money, negotiable instruments, bearer bonds or coupons, stamps, bank or currency notes'. The High Court dismissed JLT's claim holding that it was a claim for 'loss of moneys' brought about by Razak's dishonest conduct; that 'loss of money' was expressly excluded under the optional extension clause and that that phrase could not be restrictively interpreted to mean only loss of

physical money but included financial loss. In the instant appeal, JLT contended that the phrase 'loss of money' could only mean loss of physical money and not financial loss as the latter interpretation defeated the very purpose/object of the insurance policy, specifically the optional extension clause for which cover of risk JLT had paid additional premium. JLT said claims arising from the dishonest conduct of its employees would naturally cause financial loss and to deny indemnity for such claims, when that was the very purpose for which the policy was purchased, made no commercial sense.

Held, allowing the appeal, setting aside the orders of the High Court and entering judgment for the appellant:

(1) The construction placed by the High Court on the optional extension clause effectively deprived the clause of any relevance to the insured. The reasoning of the High Court effectively meant all forms of financial loss would fall outside the ambit of the optional extension thereby depriving the appellant of the peril it had insured against. The flaw in this reasoning was that in all cases of dishonest conduct there was bound to be financial loss (see para 34).

(2) The only manner to reconcile the optional extension clause with exclusion cl 1(b) of the policy was to focus on the nature of the claim of the victim against the insured bearing in mind that exclusion cl 1(b) made it clear that without the optional extension clause, the insured would not be indemnified in respect of claims directly arising out of the fraudulent acts of the insured's employees, such as Razak (see para 34).

(3) The emphasis had to be on the nature of the claim of the insured's client. It had to be so because the optional extension clause only operated in respect of claims where the insurers were not liable in the first place under exclusion cl 1(b). Accordingly, the foremost consideration ought to have been who was the victim of Razak's dishonest conduct (it was not the insured but its client, the bank) and whether the claim of the client of the insured fell within cl 1(b) of the policy so as to invite the operation of the optional extension clause (see paras 32–34).

(4) The trial judge had unduly concentrated on the words 'loss of money' and whether those words should be accorded the limited meaning of physical loss of money or the wider meaning of financial loss (see para 31).

[Bahasa Malaysia summary

Perayu ('JLT') ialah broker insurans yang telah membeli polisi insurans indemniti profesional daripada responden untuk menanggung rugi jika tuntutan dikemukakan terhadap JLT oleh pelanggannya. Pekerja JLT ('Razak') secara menipu telah menyebabkan pelanggan JLT, sebuah bank, untuk membayar lebih premium insurans yang telah masuk ke dalam akaun pihak

ketiga yang mana Razak mempunyai akses. Apabila mendapati ada penipuan, bank itu telah menuntut dan mendapat balik daripada JLT lebihan premium ia telah dibayar. JLT mohon untuk indemniti daripada responden tentang tuntutan bank tersebut tetapi responden menolak liabiliti yang membawa kepada tindakan ini. Penentuan berhubung pertikaian antara pihak-pihak di bawah A 14A Kaedah-Kaedah Mahkamah 2012 membawa kepada pembentukan polisi indemniti profesional. Fasal 1(b) polisi memperuntukkan bahawa JLT tidak boleh diindemnifikan jika tuntutan dibuat terhadapnya adalah, antara lain, membawa kepada atau menyumbang kepada 'dishonest, fraudulent, criminal, malicious or deliberate act, error or omission' JLT. Fasal itu juga memperuntukkan bahawa tiada indemniti untuk tuntutan yang dibuat untuk 'loss of money' dan butiran spesifik lain yang dalam jagaan atau kawalan JLT. JLT telah membeli fasal lanjutan pilihan yang memperuntukkan bahawa fasal 1(b) tidak terpakai di mana tuntutan dibuat terhadap JLT timbul daripada atau menyumbang kepada 'by the dishonest, fraudulent, malicious or deliberate conduct' pekerjanya. Fasal lanjutan pilihan itu, bagaimanapun, tidak meliputi tuntutan 'arising out of or in connection with loss of money, negotiable instruments, bearer bonds or coupons, stamps, bank or currency notes'. Mahkamah Tinggi menolak tuntutan JLT dan memutuskan bahawa ia adalah tuntutan untuk 'loss of moneys' yang wujud akibat perlakuan tidak jujur Razak; bahawa 'loss of money' itu jelas dikecualikan di bawah fasal lanjutan pilihan dan bahawa istilah tersebut tidak ditafsirkan secara terhad untuk bermaksud hanya kerugian wang fizikal tetapi termasuk kerugian kewangan. Dalam rayuan ini, JLT menegaskan bahawa istilah 'loss of money' hanya boleh bermaksud kerugian wang fizikal dan bukan kerugian kewangan kerana pentafsiran kerugian kewangan tidak memenuhi tujuan/matlamat polisi insurans, khususnya fasal lanjutan pilihan yang meliputi risiko JLT bayar premium tambahan. JLT menyatakan tuntutan yang timbul daripada perlakuan tidak jujur pekerjanya secara semulajadi menyebabkan kerugian kewangan dan untuk menafikan indemniti bagi tuntutan tersebut, walhal itu adalah tujuan sebenar polisi tersebut dibeli, yang tidak mempunyai sifat komersial.

Diputuskan, membenarkan rayuan, mengetepikan perintah Mahkamah Tinggi dan memasukkan penghakiman untuk perayu:

(1) Pementukan yang diletakkan oleh Mahkamah Tinggi ke atas fasal lanjutan pilihan secara berkesan menafikan fasal itu berhubung apa-apa relevan kepada orang diinsuranskan. Alasan Mahkamah Tinggi secara berkesan bermaksud semua bentuk kerugian kewangan akan terjatuh di luar skop lanjutan pilihan yang menafikan perayu terhadap bahaya ia telah diinsuranskan. Kecacatan dalam alasan ini adalah bahawa semua semua kes perlakuan ketidakjujuran terikat dengan kerugian kewangan (lihat perenggan 34).

(2) Satu-satunya cara untuk menyatukan fasal lanjutan pilihan dengan fasal

pengecualian 1(b) polisi tersebut adalah untuk memberi fokus kepada sifat tuntutan mangsa terhadap orang yang diinsuranskan dengan mengambil kira bahawa fasal 1(b) telah menjelaskan tanpa fasal lanjutan pilihan itu, orang yang diinsuranskan tidak akan menanggung rugi berkaitan tuntutan itu secara langsung yang timbul daripada tindakan penipuan pekerja orang yang diinsuranskan, seperti Razak (lihat perenggan 34).

(3) Penekanan perlu terletak pada sifat tuntutan pelanggan orang yang diinsuranskan itu. Ia perlu begitu kerana fasal lanjutan pilihan hanya beroperasi berkaitan tuntutan di mana orang yang diinsuranskan tidak bertanggungjawab pada mulanya di bawah fasal pengecualian 1(b). Berikutan itu, pertimbangan yang utama sepatutnya adalah siapa yang merupakan mangsa perlakuan tidak jujur Razak (ia bukan orang yang diinsuranskan tetapi pelanggannya, bank itu) dan sama ada tuntutan pelanggan yang diinsuranskan terangkum dalam fasal 1(b) polisi tersebut agar dapat mengundang operasi fasal lanjutan pilihan (lihat perenggan 32–34).

(4) Hakim perbicaraan telah terlalu menumpukan perhatian pada 'loss of money' dan sama ada perkataan-perkataan tersebut perlu diberi maksud yang terhad bagi kerugian fizikal wang atau maksud yang lebih luas daripada kerugian kewangan (lihat perenggan 31).]

Notes

For a case on exemption clause, see 8(1) *Mallal's Digest* (5th Ed, 2015) para 60.

Cases referred to

Malaysia British Assurance Bhd v Syarikat Pembenaan Karun Sdn Bhd [2008] 6 MLJ 533, CA (folld)

Perembun Consortium (a joint venture between Perembun (M) Sdn Bhd and Road Builder (M) Sdn Bhd) & Anor v AXA Affin General Insurance Bhd (formerly known as AXA Affin Assurance Bhd) [2011] 6 MLJ 719, HC (folld)

Rouleston Clarke Pty Ltd (in liquidation) v FAI General Insurance Company Ltd [2000] TASSC 63, SC (refd)

Legislation referred to

Rules of Court 2012 O 14A

Appeal from: Civil Trial No 22NCC-97–01 of 2013 (High Court, Kuala Lumpur)

Lim Kian Leong (Paul Ngooi and Kenneth Liew with him) (Lim Kian Leong & Co) for the appellant.

K Korinavathi (Satha & Co) for the respondent.

Anantham Kasinather JCA (delivering judgment of the court):

INTRODUCTION

[1] This was an appeal against the decision of the High Court which had dismissed the appellant-plaintiff's claim brought against the respondent-defendant under the terms of a policy of insurance, to wit, a *Professional Indemnity Policy for Insurance Brokers* No: 12DHQ/LNDZ78662 issued on 04 December 2012 ('the policy').

[2] To best capture the context of the dispute between the parties, the appellant-plaintiff will be referred to in this judgment as ('the insured') whilst the respondent-defendant as ('the insurer').

BRIEF FACTS

[3] The insured provided general insurance and brokering services. The insurer on the other hand was in the business of underwriting general insurance risk for brokers and other professionals.

[4] Under the terms of the policy, the insurer agreed to indemnify the insured against claims brought against the insured of which notice to the insurer had been given during the validity of the policy, namely from 1 January 2012 to 31 December 2012.

[5] The insured notified the insurer on 9 March 2012 of a potential claim under the policy. The insurer however repudiated any liability and cited several reasons for the position taken by them.

[6] The insured's claim under the policy could be traced to certain fraudulent acts committed by an employee of the insured, one Abdul Razak bin Abdul Ghani ('Razak') principally as against a client of the insured. The essential aspects of the fraud in summary was as follows:

(a) Razak induced the insured's client Affin Bank Bhd ('the bank') by use of forged and falsified documents to pay inflated premiums to the insured (for policies of insurance taken out by the bank) purportedly to fund certain 'risk management programmes', allegedly to be organised by the insured;

(b) Razak then diverted these additional premium payments into third party accounts to which Razak had access. This was perpetrated on the insured by inducing the insured to issue cheques based on forged letters.

The payments made by the insured were to event management companies supposedly for the holding of the 'risk management programmes';

(c) the fact was that the 'risk management programmes' were entirely fictitious and none did take place;

(d) upon discovery of the said deception, the bank demanded from the insured a repayment of the overpaid premium sum. The insured subsequently paid the bank the sum of RM1,096,372.01 as refund of all the additional premium paid to and received by the insured; and

(e) as the insurer has repudiated liability, the insured then commenced this action to recover from the insurer the said sum by way of indemnity under the terms and conditions of the policy.

[7] At the High Court, the parties agreed (on the urgings of the learned trial judge) to an O 14A process (O 14A of the Rules of Court 2012) to resolve the dispute as between them, since the essential facts were not substantially in dispute.

[8] Although initially four questions of law were drawn up for the determination of the court, the parties finally only retained two of the said issues. They were:

Question 1: Whether the loss of monies claimed by the Plaintiff ('Insured') as a result of the Risk Management Programs does or does not fall within Optional Extension Clauses of the Policy.

Question 2: Whether the payments to the individual event management companies falls within the Optional Extension Clause of the Policy.

[9] It was not in dispute that the bank was the victim of the fraud committed by Razak, an employee of the insured as there was no 'risk management programme' ever planned or organised by or for the insured. Both the bank and the insured had been deceived by Razak. The insured had to consequently repay the bank the overpaid premium.

The insurer agreed to abandon all other defences that they had raised as grounds for the refusal to indemnify the insured under the policy. They restricted their denial of liability purely to the outcome of the two questions which revolved basically on the construction to be accorded to relevant terms of the policy, and more specifically, the optional extension, Option 1– amendment of dishonesty extension clause. ('Option 1– extension').

The policy/optional extension clauses

(Option 1 – amendment of dishonesty exclusion)

[10] The material portions of the policy, for consideration, were:

POLICY SCHEDULE

INSURANCE BROKER PROFESSIONAL INDEMNITY

Policy No: 12DHQ/LNDZ78662

...

...

...

OPTIONAL EXTENSION

1) DISHONESTY OF EMPLOYEE

...

...

PROFESSIONAL INDEMNITY POLICY

FOR INSURANCE BROKERS

INSURING CLAUSES

...

...

The Company agrees, subject to the following limitations, terms and conditions and subject to any policy endorsements:

1. To indemnify the Insured against any Claim which may be made against the Insured and notified to the Company during the period of insurance stated in the Schedule:

   (a) For actual or alleged breach of professional duty in the profession of Authorised Insurance Broker; or

   (b) ...

...

...

EXCLUSIONS

1. This policy shall not indemnify the Insured in respect of any Claim or Claims made against them:

   (a) ...

(b) brought about or contributed to by the dishonest, fraudulent, criminal, malicious or deliberate act, error or omission of the Insured (and/or any company or entity which has a beneficial interest in the Insured) of their predecessors in business; or

(c) ...

(d) for loss of money, negotiable instruments (including shares), bearer bonds or coupons, stamps, bank or currency notes in the care or custody of the Insured; or

(e) ...

(f) ...

(g) ...

(h) ...

...

...

...

OPTIONAL EXTENSION CLAUSES

Option 1 – Amendment of Dishonesty Exclusion

If a limit for this Extension is specified in the Schedule, Exclusion 1(b) shall not apply in respect of Claims for damages for breach of professional duty arising out of or contributed to by the dishonest, fraudulent, malicious, or deliberate conduct of the Insured's employees (but not including any partner, director or controlling officer). However, no indemnity will be provided to any person committing or condoning such dishonest, fraudulent, malicious, or deliberate act(s).

This extension does not cover claims arising out or in connection with for loss of money, negotiable instruments, bear bonds or coupons, stamps, bank or currency notes.

Option 2 – Automatic Reinstatement

...

...

The High Court

[11] At the High Court, *the insured contended* that they were entitled to be indemnified under Option 1 – extension since the essential ingredients thereto required, namely, that the claim arose in the context of their professional duty to the bank and that the loss was directly caused by a dishonest or fraudulent act of an employee ('Razak'), had been satisfied.

As regards to the proviso or limitation of the extended cover under Option 1 –

extension, worded in the following terms:

> This extension does not cover claims arising out or in connection with for loss of money, negotiable instrument, bear bonds or coupons, stamps, bank or currency notes.

it was submitted that the construction of the words 'loss of money' therein stated should be restricted to loss of physical cash or its equivalent (similar to bearer bonds, shares, etc).

[12] It was further argued for the insured that the extension had been purchased to expressly overcome the effect of exclusion 1(b) of the policy (as confirmed by the reference – *extension 1(b) shall not apply* ... in the body of Option 1 – extension) and if the meaning to be given to the words 'loss of money' was more extensive or wider than 'physical cash', it would lead to an absurd or illogical result, namely excluding recovery of all losses of whatsoever financial nature or consequence. The proviso or the exclusion of 'loss of money' must of necessity therefore mean only loss of physical cash (akin to insurance taken to cover loss of cash in transit, breach of fidelity of employee etc).

[13] Further, relying on the decisions in *Perembun Consortium (a joint venture between Perembun (M) Sdn Bhd and Road Builder (M) Sdn Bhd) & Anor v AXA Affin General Insurance Bhd (formerly known as AXA Affin Assurance Bhd)* [2011] 6 MLJ 719 and *Malaysia British Assurance Bhd v Syarikat Pembenaan Karun Sdn Bhd* [2008] 6 MLJ 533 (FC), it was contended for the insured that even if a clause in the insurance policy was open to two or more possible interpretation, the court should in such instance prefer a ruling against the insurer and in favour of the insured based on the *'contra proferentum'* rule of construction.

[14] It was the *insurer's contention on the other hand* that the words of the proviso or limitation to Option 1 – extension was free of any ambiguity and therefore ought to be given its clear and literal meaning and effect. It was argued for the insurer that in substance the insured's claim was for loss of monies (that is, loss in terms of financial value) and by force of the proviso or limitation to the extension, the insured who was claiming for financial loss, was not entitled to be paid at all under the policy.

[15] A further point canvassed by the insurer was that the loss sought by the insured to be indemnified under the policy was in substance a repayment of overcharged premium and this did not in any case fall within the terms of the policy.

[16] The insurer's counsel also referred to the decision of the Supreme Court of Tasmania in *Rouleston Clarke Pty Ltd (in liquidation) v FAI General Insurance*

Company Ltd [2000] TASSC 63 where the court (endorsing the court of first instance) had the opportunity to consider a proviso or limitation to the extension clause, almost in identical words to that utilised in the policy in this instant case. The court there had held that the term 'loss of money' included within its purview any detriment or disadvantage suffered as a consequence of being deprived of the benefit of any of the items specified in the provision in question, *regardless of whether they had been physically destroyed or mislaid*; in other words it was not hinged to physical loss *of money* only.

LEARNED TRIAL JUDGE

[17] The learned trial judge having considered the respective contentions of the parties answered both the questions posed to the court, in the negative and accordingly proceeded to dismiss the insured's claim.

[18] The learned trial judge in arriving at the aforesaid decision was persuaded to a large extent by the reasoning of the Tasmanian Supreme Court on the almost similarly worded proviso or limitation found in the *Rouleston Clarke* case. The judgment there in that case had also more importantly ruled that there was no ambiguity in the words used; 'loss' as found therein ought to be accorded its natural and ordinary meaning in the specific context of the intended cover under an insurance policy.

[19] The learned trial judge in Her Ladyship's judgment posed the real issue that was before the court in the following manner:

> The relevant words for the purposes of the instant case are 'loss of money'. Should the phrase be accorded a restricted definition, namely the loss of physical money only, or should it be accorded a broader construction so as to encompass financial loss etc.

[20] The learned trial judge was of the view that construing the phrase in the manner suggested by the insured would require the court to insert or read into the proviso or limitation, the word *physical*, thereby effectively amending it to read – 'This extension does not cover claims ... for physical loss of money ...'. In Her Ladyship's view there was no basis to give it such a strained construction to meet the facts of this case; the court had no function to add, amend or vary the terms that was expressly set out and which bound the parties.

[21] Her Ladyship further noted:

> (iv) If the parties had intended to cover only physical loss of monies or financial instruments, then this should have been and would have been clearly stipulated. There is a considerable difference between 'loss' and 'physical loss'. The latter envisages that the money or financial instrument is lost or misplaced or disappears. However 'loss'

> encompasses a wide variety of events including a shortfall or deficiency or debit or deficit of money albeit from theft of monies or loss of a financial benefit by reason of the loss of a financial instrument, rather than the physical loss of the instrument itself. Loss also routinely encompasses damage and injury in a variety of insurance policies. Given the wide discrepancy between the definitions, it would have been incumbent upon parties to specify that loss was restricted to a physical loss;

[22] It was also held that there was no justifiable reason for 'physical loss' to be deemed as an implied term of the contractual relationship, based, either on the legally recognised 'commercial necessity' test or of the 'official bystander' test. The learned trial judge went on to further state:

> This is particularly, given that the word 'loss' is routinely utilised in insurance policies to encompass a wide variety of matters from financial deficit to injury and harm. It is regularly utilised to designate financial loss or damage.

[23] Finally at para 61 of the judgment of the High Court, the learned trial judge held as follows:

> Ultimately *whether the loss is considered as having arisen at the point when the Bank made the payments to the Plaintiff* or the *monies were diverted from the Plaintiff into third party accounts* by the dishonest machinations of Razak, the loss is a financial loss. The financial loss was suffered by the Bank and was reimbursed by the Plaintiff. This claim is therefore a claim arising from financial loss suffered by a client in respect of which it sought reimbursement from the Plaintiff as the financial loss arose by reason of the dishonest acts of the Plaintiff's employee. However *it cannot be disputed that at all times the basis of the claim was a loss of moneys brought about by the dishonest conduct of Razak.* (Emphasis added.)

BEFORE US

[24] Firstly, the case for the insurer. Counsel argued that the proviso or limitation to the Option 1 – extension was clear and no issue arose as to any ambiguity or uncertainty in the meaning of the word 'loss of money' as found there. The Option 1 – extension was specifically to negate the effect of exclusion cl 1(b) and as an experienced insurance broker, the insured ought to have been aware of the wide reach of the limitation as found in the proviso to the extension.

[25] It was further contended for the insurer that the restricted reading advocated by the insured in this case, to limit 'loss of money' to mean only physical money, was tantamount to contending that the exclusion as found in exclusion cl 1(d) was intended to be duplicated. Exclusion cl 1(d), was as noted earlier still intact and operative in this case as there was no optional extension

to nullify the same. Exclusion cl 1(d) stated that there would not be any indemnity for '... loss of money, negotiable instrument (including shares), bearer bonds or coupons, stamps, bank or currency notes *in the care or custody of the insured; or*' (Emphasis added), clearly denoting it was to cover loss of physical money in the hands of the insured.

[26] Hence, it was submitted that the 'loss of money' used in the proviso or limitation to Option 1 – extension could not also mean physical money; it necessarily had to be something beyond that.

The intention of the policy (when construed as a whole) it was argued, was simple and 'clear enough and there was therefore no room for any '*contra proferentum*' rule or for any logical interpretation to be applied in this instance.

[27] The insured repeated the main grounds that had been previously canvassed before the High Court. It was argued that the learned trial judge's construction of the phrase 'loss of money' effectively defeated the very purpose or object of the insurance policy itself and more specifically the Option 1 – extension, for which cover of risk, additional premium had been paid by the insured. The reference 'loss of money' in the proviso or limitation to the extension, it was argued, could therefore only mean loss of physical money and did not extend to loss of a financial value occasioned to the insured, as construed by the High Court.

[28] The counsel for the insured submitted further that although the High Court was right to perhaps take into consideration the reasoning found in *Rouleston Clarke*'s case, the learned trial judge had overlooked that Crawford J had also cited in that judgment various instances where such proviso or limitation would not apply.

One of the examples set out in particular was where an employee deliberately and maliciously caused a client to pay excessive tax (the insured in that case was in the business of tax agents) and such limitation did not apply. It was argued that Razak's action in inducing the bank to pay 'excessive premiums', in our case, would fall squarely within such a stated exception and the learned trial judge had failed to direct her attention thereto.

[29] One other point of some significance put forward by the counsel for the insured was that the very purpose of the Option 1 – extension was to provide cover for risks ' ... arising out of or contributed to by the dishonest, fraudulent, malicious or deliberate conduct of insured, employees ... ', and the normal and natural consequence or any such breach or lapse was in any event 'financial loss'. In the circumstances to deny that coverage (by construing 'loss of money'

as all pervading including loss of financial value) would make no commercial sense and make such coverage clearly intended in this situation, totally worthless.

In so doing, the learned trial judge, it was argued, had excluded the *very peril or risk* intended to be covered and in its place misplaced her emphasis on to the consequences of such a risk, when she dismissed the insured's claim.

JUDGMENT OF THE COURT

[30] In our judgment, the ratio of the decision of the Supreme Court of Tasmania in the case of *Rouleston Clarke Pty Ltd (in liquidation) v FAI General Insurance Company Ltd* [2000] TASSC 63 is that pronounced by the court in para 25 of the judgment of the court. This reads as follows:

> I reject the Plaintiff's contention that 'loss' should be construed as meaning a physical loss which does not encompass a loss arising from Mr Badger's conversion of the clients' negotiable instruments to his own use. The meaning of loss includes detriment or disadvantages from being deprived of the benefit of any of the specified items regardless of whether they have been physically destroyed or mislaid. The detriment suffered as a consequence of Mr Badger's conduct is such a loss. I accordingly conclude that as a consequence of the proviso to the dishonestly extension, the claims are excluded from cover by that extension.

[31] With respect, in our judgment, learned counsel for the respondent and the learned trial judge misunderstood the ratio of the decision of the court by unduly concentrating on the words 'loss of money' and whether these words should be accorded the limited meaning of physical loss of money or the wider meaning of financial loss. With respect, in our view, this focus on the meaning of the words 'loss of money' caused Her Ladyship to disregard the pronouncements in the same judgment of the court that the proviso only applies where the detriment or disadvantage suffered by the insured arises from being 'deprived of the benefit of any of the specified items regardless of whether they have been physically destroyed or missing'. Our understanding of the ratio of the judgment of the Tasmanian Supreme Court is that a pre-requisite to the applicability of the proviso is that the loss (physical or otherwise) must concern one of the specified items listed in the proviso. Our view to this effect is reinforced by the pronouncements contained in para 20 of the same judgment of the court to the following effect:

> *In construing the proviso, it is to be borne in mind that it relates to claims for damages for the loss of specified items.* Claims for damages are only made where a financially measurable loss has been suffered. Whilst the physical loss of some of the specified items, such as bank or currency notes, will cause a financial loss, that is not always the case with some of the other items such as negotiable instruments. When a negotiable instrument is physically lost, for example, destroyed or mislaid, it may readily be replaced without any financial loss. *It is when the negotiable instrument is*

> *converted to the use of another that financial loss is suffered.* This suggests that loss means more than physical loss. Support for this suggestion comes from a consideration of the conduct which must give rise to the loss referred to. That conduct is the 'dishonest, fraudulent, criminal or malicious conduct of employees'. Whilst physical loss of the items referred to can arise from conduct of this description, the sort of loss which is more readily linked to this sort of conduct is a detriment or disadvantage arising from the appropriation of the specified item to the use of an employee. (Emphasis added.)

[32] The net effect of the highlighted portions of the judgment of the Supreme Court of Tasmania is that the proviso only operates to preclude the insured from being indemnified by the insurer in cases where at the point of loss/misappropriation of any of the specified items listed in the proviso by an employee of the insured, the items either belonged to the insured or were in the custody of the insured. Our rationale for this construction of the proviso is that in cases where an employee of the insured misappropriates or loses one of the specified items listed in the proviso, then, the loss is that of the insured and not the client of the insured. In a fact situation of this nature, the insured cannot demand to be indemnified by the insurer because the optional extension clause only exists to indemnify the insured where the client of the insured has been defrauded by the fraudulent conduct of the employee when performing his duties on behalf of the insured and not to cases where the insured has been defrauded by his own employee. In other words, the emphasis should be on the nature of the claim of the client of the insured. This must necessarily be so, in our opinion, because the optional extension clause only operates in respect of claims where the insurers are not liable in the first place under exclusion cl 1(b). Hence, the pronouncement by the judge of first instance in the *Rouleston Clarke*'s case that:

> The question for my determination in relation to each claim is whether it is denied cover by exclusion (b) as being a 'claim ... for ... dishonest, fraudulent ... criminal or malicious ... acts or omissions ... of the insured's ... employees?

[33] Accordingly, in our judgment, the foremost consideration when answering the two questions ought to have been, who was the victim of the dishonest conduct of Razak and whether the claim of the client of the insured fell within cl 1(b) of the policy so as to invite the operation of the optional extension clause. In our respectful view, the answer to both questions should have been in the positive upon a consideration of the aforesaid two factors. First, the modus operandi of Razak as highlighted in para 6 of this judgment was to misrepresent the client's obligations as regards monies due from the client to the insured. Following such misrepresentation, Razak misappropriated monies paid by the client of the insured but clearly not due to the insured. Secondly, to the extent the monies paid by the client bank (on the facts of this case) to the insured were not lawfully due to the insured, the monies could not be said to belong to the insured. In other words, the victim

of the fraud perpetrated by Razak was not the insured but its client, the bank. Thirdly, it is evident that any claim for the recovery of the excess premiums by the client against the insured would have been based on the dishonest conduct of Razak and to that extent the claim would clearly fall within cl 1(b) and consequently avoid liability on the part of the respondent insurers but for the optional extension clause. This has to be contrasted with the situation in *Rouleston Clarke*'s case where the claim of the victim was for the failure of the insured to account for the negotiable instruments and consequently outside the ambit of cl 1(b) (see para 15 of the judgment of the Supreme Court of Tasmania).

[34] In our judgment, the construction placed by the High Court on the optional extension clause would effectively deprive the extension option of any relevance to the insured. We opine to this effect because the reasoning of the High Court effectively meant that all forms of financial loss would fall outside the ambit of the optional extension thereby depriving the appellant of the peril that it had insured against. With respect, the flaw in this reasoning is that in all cases of dishonest conduct there is bound to be a financial loss. Accordingly, in our judgment, the only manner to reconcile the optional extension clause with exclusion cl 1(b) of the insurance policy is to focus on the nature of the claim of the victim against the insured bearing in mind that exclusion cl 1(b) makes it clear that, without the optional extension clause the insured would not be indemnified in respect of claims directly arising out of the fraudulent acts of employees, such as Razak.

[35] We are fortified in our conclusion that on the facts of this case, the appellant insured is entitled to be indemnified by the example provided by Crawford J in the decision of the Tasmanian Supreme Court. In para 25 of His Lordship's judgment, His Lordship expressed the view that one instance where the claim of the insured would fall within the ambit of the optional extension clause would be where 'an employee deliberately and maliciously causing a client to pay excessive tax (the appellant carried on the business of tax agent)'. Similarly, in our case, the appellant insured was in the business of insurance broking. In other words, the appellant placed and arranged insurance for its clients. The dishonest Razak caused the client of the appellant to overpay the actual insurance premiums, which he then proceeded to fraudulently appropriate to his own benefit. Upon the said fraud being discovered, the victim bank client demanded and obtained the excess premiums from the appellant. In our judgment, the facts of our case fall within the four corners of the example furnished by Justice Crawford.

For the reasons contained in this judgment, we allow the appeal with costs and set aside the orders of the High Court. We order that there be judgment for the appellant in terms of prayers (a) and (b) of the statement of claim. The

respondent is hereby ordered to pay the sum of RM40,000 as costs here and below to the appellant. The deposit is hereby refunded to the appellant.

Appeal allowed, orders of the High Court set aside and judgment entered for the appellant.

Reported by Ashok Kumar